

Docket No. RM2009-1

Time Warner Inc. (Time Warner) respectfully submits the following comments in reply to the initial comments of the Public Representative (PR) regarding proposed modification number 9 in Docket No. RM2009-1.¹ Modification 9 would use an overall CRA adjustment in the Periodicals model, similar to the adjustments that are used in worksharing models for other classes. It would replace the method used in ACR2007, which assumed, despite clear evidence to the contrary, that no adjustment was needed in the modeled piece-sorting costs and that the entire weight of the overall CRA adjustment therefore should be applied to the part of the model that represents bundle and container costs.

¹ Public Representative Initial Comments Related to Postal Service Flat Cost Models (filed December 1, 2008).

1. Use of a single overall CRA adjustment is a reasonable compromise, given imperfect data, between the “ideal” approach and the method used in ACR2007.

As Time Warner has pointed out previously, and as can also be verified from the spreadsheet that accompanies the current Postal Service proposal, the method used in ACR2007 had two unfortunate effects: it caused a substantial understatement of total piece-sorting costs, and a large overstatement of the costs associated with bundles, sacks and pallets.² The distortion caused by continuing that approach would be made even more severe by the other model changes that the Postal Service has proposed in this docket.³

The PR appears to argue (at 5) in favor of using several different CRA adjustments applied to different parts of the model, because:

use of one system level adjustment factor would distort unit costs and, more importantly, unit cost differences for purposes of setting worksharing discounts.

But the PR also appears to think that, until the use of several different CRA adjustments has been fully investigated, the Commission should disallow any change from the FY2007 method, because he believes that:

the procedure advocated by the Postal Service in this modification is likely to distort estimated unit costs for

² See Docket No. ACR2007, Initial Comments of Time Warner Inc. on FY 2007 Annual Compliance Report (filed January 30, 2008), at 11-14; and Docket No. RM2008-2, Initial Comments of Time Warner Inc. in Response to Order No. 99 (September 8, 2008), at B3-B5, B14-B15.

³ In the original ACR2007 model, the effect of this approach was to multiply the non-piece costs (i.e., bundle and container costs) by a factor of 1.207, in spite of evidence that the unadjusted model costs for those items might already be slightly higher than the CRA costs. See Second Notice of the United States Postal Service of Minor Revisions to Materials Accompanying Its FY 2007 Annual Compliance Report -- Errata (Items 10, 11) and spreadsheet 'PER OC flats 07ACRv011608 errata.xls' (filed January 18, 2008). But with the other model changes proposed in this docket, the modeled non-piece costs would be multiplied by a factor of 1.302.

Periodicals worksharing categories to an unknown degree.

Id. at 3.

In principle we agree with the PR that it would be desirable, if sufficiently detailed CRA data were available, to use different CRA adjustments for different groups of unit costs. And the Periodicals model does identify separately the model costs that relate directly to piece sorting, and the corresponding CRA costs. In the Postal Service's current proposal, total modeled annual Outside County piece sorting costs are \$432 million (cell f92 in worksheet 'CRA Flats'). And while the CRA cost pools may be less than perfectly "pure," as the Postal Service argues, the best estimate available from the model is that the corresponding CRA costs are \$584.7 million (cell 'CRA FLATS'!g92). That would indicate that the modeled piece sorting costs should be modified by a factor equal to $584.7/432 = 1.3535$. Similarly the remaining modeled costs are \$637.74 million, versus CRA costs of \$677.41 million (cells 'CRA COSTS'!f98-g98). That would indicate an average CRA adjustment for non-piece costs equal to only 1.062.

These results are very different from those that follow from the previous method, under which piece-sorting costs would not be adjusted at all and other costs would be adjusted by a factor equal to 1.302.

The Postal Service's proposed solution, namely to use an overall adjustment equal to 1.1798 for both piece-sorting and other modeled costs is a reasonable compromise, at least for the present time. We urge the Commission to approve that approach.

2. The CRA adjustment in the Periodicals model is the least likely to cause significant distortions.

The PR's concern about possible distortions caused by an overall CRA adjustment appears to be focused on the Periodicals flats model. But for reasons described below, that is the model where such concerns are the least warranted.

Unlike the flats models used for other mail classes, the Periodicals model explicitly models all activities that correspond to the costs used in the CRA adjustment. For example, it explicitly models the movements, sortation and opening of containers and bundles, whereas the other models do not. The Periodicals model contains no assumption about costs not modeled behaving in a manner proportional to the costs that are modeled.

It is therefore no surprise that the Periodicals CRA adjustment factor is much closer to a value of one than the proportionality factors used in the First Class and Standard models. It follows from the fact that those other models extend the CRA adjustment to costs of activities not explicitly modeled, e.g. movements of containers on the platform, assuming that those costs are affected by characteristics such as presort levels in a manner proportional to the costs that are explicitly modeled.⁴ The Commission therefore should be the least concerned by the Periodicals model CRA adjustment, since it is the least likely to cause any significant cost distortion.

On the other hand, since the Periodicals model explicitly models all the costs represented in the CRA adjustment, one might expect a perfect model to have a

⁴ In Docket No RM2009-1, the CRA adjustment factors used in the First Class and Standard flats models are 2.436 and 1.725, versus only 1.1798 in the Periodicals model.

CRA adjustment that approaches one. As long as it is significantly different from one, there should be an ongoing effort to determine why and to make any needed corrections. The fact that modeled non-piece costs are reasonably close to the corresponding CRA costs is an encouraging sign, indicating that that part of the model on the whole is a reasonably accurate representation of reality.

But the large difference between modeled piece sorting costs and those shown by the CRA indicates the need for further analysis. The discrepancy could point to inefficiencies that need to be corrected, or it could indicate the need to modify the model to be more consistent with operational reality.

It remains unknown at this time what the numbers resulting from FY2008 data will look like. But if, as in the FY2007 model, the CRA piece sorting costs for Periodicals flats once again exceed the model's prediction of what those costs should be, then efforts should be directed in the coming year at finding the causes for those discrepancies and correcting them.

Respectfully submitted,

s/

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